Claiming only allowable compensation is tricky. It requires a decent amount of analysis. One of the trickier aspects of the compensation analysis is understanding that the compensation ceiling changes over time. One may also need to understand that the compensation ceiling applies to different groups of employees, or even different groups of customer contracts, depending on the year in which the costs were recorded (and/or the year in which the contract was awarded).

And this doesn't really even apply to challenges to compensation reasonableness. That's a whole 'nother thing. No, we're simply talking about compliance with FAR 31.205-6(p). It's tricky, and contractors are required to get it right.

It's so tricky, that DCAA has so far failed to issue comprehensive guidance to its auditors via the Selected Areas of Cost Guidebook. **Chapter 10** of the Guidebook (Compensation for Personal Services) is "under construction," and has been that way for years.

Nonetheless, it is DCAA's position that a contractor who claims compensation costs in excess of the 31.205-6(p) ceiling(s) has claimed an expressly unallowable cost. (See the Contract Audit Manual at 6-414.8.) Recently, this position was put to the test at the Armed Services Board of Contract Appeals (ASBCA).

Ology Bioservices, Inc. (Ology) **appealed** a Contracting Officer Final Decision applying a penalty for Ology's inclusion of claimed executive compensation costs in excess of the FAR ceiling in its Fiscal Year 2013 proposal to establish final billing rates, which was submitted on time six months after the close of Ology's fiscal year. However, DCAA had some issues with Ology's submission and Ology was required to fix those issues and resubmit its proposal, which it did about six months later. DCAA audited the proposal and questioned costs. After the audit report was issued, and after a "lengthy negotiation" with the DCMA contracting officer—a period that lasted nearly six years (December 2014 through May 2020)—the COFD was issued, in which the contracting officer determined that Ology had claimed executive compensation costs that exceeded the FY 2013 ceiling by $1,749,890. As Judge O'Connell of the Board wrote, "The CO found that $979,938 of this amount was allocated to covered contracts and assessed Ology a penalty in this amount. In addition, she demanded interest that brought the total government claim to $1,109,160."

In the Board's analysis of the situation, the matter was not nearly as straight-forward as DCAA

and DCMA claimed it was. Of particular import was the fact that OFPP had not published the FY 2013 compensation cap until March 15, 2016. “The government has not provided any explanation as to why there was such a delay in establishing the FY 2013 cap.”

Long-time readers of this blog know that we have complained about OFPP’s lack of diligence before. Several times. The fact of the matter is that OFPP didn’t like the ceilings that were calculated at the time, and expressed the dislike by failing to carry out the statutory duty imposed on the agency, the duty that required timely publication of the ceiling. The situation continued after the executive compensation ceiling became the contractor compensation ceiling and the new benchmarks were adopted during the Obama Administration. The situation is now so bad that even DCAA **has told** their auditors not to count on the OFPP and, instead, to calculate their own ceilings for audit purposes.

Back to Ology’s appeal.

Because the correct FY 2013 “cap” was not issued in time, the government’s position was that the FY 2012 cap applied to the costs that Ology had claimed. The rationale for that position was that, when OFPP had published the FY 2012 cap amount, the language used was ““amount applies to limit the costs of compensation for contractor employees that are reimbursed by the Government to the contractor for costs incurred on all contracts, after January 1, 2012 *and in subsequent contractor FYs*
, unless and until revised by OFPP.” (Emphasis added.) Thus, even though the statute required an annual ceiling to be calculated and published, the government argued that the last published ceiling applied prospectively, on a flat-line basis.

The Board analyzed the statute that established the executive compensation ceiling (10 U.S.C. § 2324) based on the language in place at the time it would have applied to Ology. The Board concluded that the statute required publication of an annual cap value, and that it was unreasonable to hold Ology accountable for claiming costs in excess of an outdated ceiling. To be clear, the Board agreed that Ology had claimed unallowable costs; however, the Board found that the excess costs were not expressly unallowable and that Ology should not have to pay penalties and interest on the excess amounts.

Judge O’Connell wrote—

Neither the statute nor any FAR provision specified a date by which OFPP must establish the cap. While it is reasonable to infer that Congress granted OFPP some leeway as to when it would set the cap, we do not believe that Congress intended OFPP to have unlimited time to update the cap or for the government to apply an outdated cap for years on end. … Further, the government imposed on the contractor an obligation under the Allowable Cost and Payment clause to submit its final indirect rate cost proposal within six months of the end of its fiscal year, FAR 52.216-7(d)(2). The government required the contractor to certify at that time that the proposal did not include any expressly unallowable costs, FAR 52.242-4(c). To submit the proposal and make this certification, the contractor would have to know the cap for that year. …

While it is true that OFPP eventually met the statutory directive to establish an FY 2013 cap, it did so long after it would provide guidance to contractors, at least those who complied with their contracts by submitting timely indirect cost rate proposals. Applying the FY 2012 cap to 2013 compensation would have the odd effect of placing contractors who complied with their deadlines in a worse position than a contractor who waited until after the March 15, 2016 issuance of the FY 2013 cap to submit its proposal. The Board believes that Congress expected more of OFPP than a technical compliance with the statutory directive that was too late to be helpful. …

This dispute involves FY 2013 compensation and the FY 2013 would be the cap that applies, not the FY 2012 cap. The FY 2013 cap did not exist when Ology certified its FY 2013 indirect cost rate proposal and the government has, in any event, abandoned the argument that the FY 2013 cap could be applied retroactively to Ology's FY 2013 proposal. Accordingly, there is no issue that requires a hearing. The government cannot carry its burden of demonstrating that Ology included expressly unallowable costs in its FY 2013 proposal and that a penalty was warranted. Ology is entitled to summary judgment that its FY 2013 executive compensation costs were not expressly unallowable at the time it certified its final indirect cost rate proposal because the FY 2012 cap was no longer applicable.

Although Ology won its victory, please don't see this decision as a free rein to include the full amounts of contractor compensation in your final billing rate proposals. A ceiling still exists—albeit it must be manually calculated using the existing statutory formula because OFPP cannot be arsed to do its job. Costs claimed in excess of that (manually calculated) ceiling are still unallowable.

What this decision does, however, is provide support for the argument that costs claimed in excess of that ceiling are not *expressly* unallowable.

To that extent, it’s an important decision.